

**CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM
STATEMENT OF INVESTMENT POLICY**

**FOR
CALIFORNIA URBAN REAL ESTATE**

April 14, 2003

This Policy is effective immediately upon adoption and supersedes all previous community housing and development policies.

I. PURPOSE

This document sets forth the investment policy ("the Policy") for the California Urban Real Estate (CURE) Program ("the Program"). The design of this Policy ensures that investors, managers, consultants, or other participants selected by the California Public Employees' Retirement System ("the System") take prudent and careful action while managing the Program. Additionally, use of this Policy provides assurance that there is sufficient flexibility in controlling investment risks and returns associated with the execution of real estate investment strategies.

II. STRATEGIC OBJECTIVE

Achieving the highest total rate of return for the System is the strategic objective of the Program. The System considers California urban real estate investments a component of the Specialized (or "Non Core") Equity Real Estate portfolio, and as such, they shall be required to achieve an appropriate risk-adjusted return.

CURE investments include, but are not limited to low-to-moderate-income housing, multi-family low-income housing, commercial or residential or both, urban infill, community redevelopment, and rehabilitation of core properties. The System shall make such investments under specified conditions and circumstances as described in this Policy. The structure of investment and long-term rate of return shall relate to the relative risk of the investment due to the type, nature of, and relative control over the investment. Minimum acceptable returns shall stay consistent with those defined by the Statement of Objectives and Policies for the Equity Real Estate Portfolio. Returns shall remain acceptable unless the level of risk, as a result of guarantees or subsidies, is below the level associated with other real estate investments made by the System.

III. INVESTMENT APPROACH AND PARAMETERS

A. Approach

Investment in the Program does not imply reduced expectations for returns or increased willingness to accept risk. The System shall only invest in situations where the investment risk is no greater than in other real estate investments made by the System. If the risk inherent in a particular project is unacceptably high, then the System shall require guarantees, subsidies, or other financial assistance by government agencies to reduce risk to an acceptable level.

The System shall ensure investments meet the following criteria:

1. Meet standard of prudence required of other investments, and thus affirmatively meet the prudence and “sole-interest” standard.
2. Any benefit the investment may confer on other interests is not the responsibility or within the ability or control of the System, but only of those who manage or are otherwise responsible for the target enterprise.

B. Asset Selection Criteria

The primary emphasis of the Program is in the State of California. The primary types of CURE projects covered by this Policy are outlined in the succeeding paragraph.

1. Residential, office, retail, entertainment, hotel, and mixed-use projects shall be considered. Asset selection shall be based upon traditional real estate measurements for long-term sustainability.

The System shall consider projects and development sites characterized by the following key elements:

- a. Sufficient size to create a mix of uses and critical mass;
- b. Single ownership and control;
- c. Compatible surrounding land uses and densities;
- d. Environmentally clean or manageable remediation; and

- e. Access to public and private transportation routes, housing, retail services, and amenities.
2. Other projects that may not be specifically defined below, but that benefit certain economic groups or geographic areas and meet the risk/return objectives of the System, may also be considered. This Policy addresses investments in both existing and development projects. While age- restricted housing projects are not prohibited by this Policy, they are intended to be governed by a separate policy (Statement of Objectives and Policy for Senior Housing Investments).

- a. Low-income Housing - Rental or for-sale housing projects with a portion of the units targeted for low-income or very-low income residents. (Low-income is defined as 80% of median income; very-low income is defined as 50% of the median income.)

This category may include acquisition financing for public agencies seeking to purchase “at risk” rental projects where affordability is endangered by expiring rent restrictions. The System may consider investing in for-sale projects with restricted affordability up to 120% of median income level when sponsored by a public agency attempting to promote home ownership. The System shall require financial sponsorship or other assistance by the appropriate governing public agency prior to investment.

- b. Multi-family Low-income Housing - Small group-care housing or shelters for disadvantaged groups. Additionally, this type of housing encompasses community development loan programs sponsored and subsidized by public or private entities offering low-interest loans and attractive terms to residents within a specific geographic area for neighborhood revitalization.
- c. Economic Development or Redevelopment - Commercial, industrial, mixed-use, residential development or revitalization projects that may or may not leverage public resources. Their design directly benefits businesses, employees, or residents of low-to-moderate-income areas, or underserved markets.

- d. Urban Infill and “Smart Growth” Strategy - The acquisition, development, redevelopment, repositioning, conversion, and eventual disposition of office, retail, residential, hotel, and mixed-use projects. Smart Growth encompasses assorted initiatives addressing the increasing concern of communities about suburban sprawl and its impact on communities, open space, air quality, traffic congestion, and existing infrastructure. Many of these communities are redirecting development and infrastructure investment within the existing core. The System shall seek profitable investment opportunities consistent with these trends. Such opportunities may include investment in traditional urban cores, urban infill, and suburban infill.

C. Investment Vehicles and Structures

The System shall invest in CURE projects through equity structures and investment vehicles as allowed under the appropriate sector or other appropriate Policies (e.g., Core Apartment, Retail, Office, Industrial, or Single-Family Housing Program). Similar vehicles, consistent with the System’s Hybrid Debt and Joint Venture policies, may also be acceptable. The above-mentioned Policies outline the acceptable criteria for the investment structure and vehicles.

1. For existing projects, the preferable structures include, but are not limited to, the following:
 - a. Commingled funds
 - b. Direct equity investments
 - c. Direct mortgages
2. For development projects, the preferable structures include, but are not limited to, the following:
 - a. Commingled funds
 - b. Direct equity investments
 - c. Equity joint ventures

d. Convertible participating mortgages

The System shall make investments in community housing and development projects through the assistance of investment advisors, affiliates, or partners familiar with such transactions.

D. Underwriting Criteria

Underwriting standards shall include demonstrated records of accomplishment in similar projects. Standards shall also include access to additional capital, if necessary, covering potential cost overruns, and no secondary collateral requirements unless essential. Where projects meet the underwriting criteria, the System shall consider pricing concessions to support affordability on a case-by-case basis.